Long-Term Budget Issues: Moving From Balancing the Budget to Balancing Fiscal Risk

Based on Remarks by
The Honorable David M. Walker
Comptroller General of the United States
Before the Senate Committee on the Budget
Washington, D.C.

February 6, 2001

GAO
Accountability * Integrity * Reliability

In recent testimony before this committee, Federal Reserve Chairman Alan Greenspan observed that the new, larger surplus projections have reshaped the choices and opportunities before us. That is true. As I have said before, this Administration and this Congress enter the 21st century facing new opportunities—and new challenges. You have the opportunity to respond to many of today's wants, but also the obligation to address several major challenges that loom on the horizon.

As you face budget choices in a time of projected surpluses, I'd like to make a few key points about the long-term fiscal policy challenges facing this Congress and our nation.

First, as the Congressional Budget Office (CBO) acknowledges, its projections are based on a set of assumptions that may or may not hold. Second, although higher surplus projections provide room to address pent-up demands for some tax cuts and additional spending, it is important to remember that the long-term outlook looks worse primarily because of revised estimates of long-term growth in health care costs. Third, higher surpluses present new challenges in saving for the future as we approach a time when there may be almost no publicly held debt to retire and when the personal savings rate has plummeted. Fourth, GAO's long-range budget simulations show that, even if the assumptions used by CBO about productivity increases and spending constraints are realized, the federal budget will return to the days of red ink because of known demographic trends and rising health care costs.

In making budget choices, we need to do more than just focus on today. We must also think about tomorrow. Why? Because at the moment, we can afford to take a range of actions that may not be possible in the future. As a result, today's budget choices should be viewed in terms of a portfolio of fiscal options. In the aggregate, choices should be balanced across different levels of fiscal risk to the long-term budget outlook. Attention must be paid not only to responding to current needs but also to making decisions—particularly when it comes to promoting long-term growth and reducing the relative future burden of entitlement programs—that will preserve the ability of future generations to make their own choices.

Before looking ahead, I think it's useful to take a moment to reflect on how we got where we are today.

We face burgeoning surplus projections not only because of sustained economic growth but also as a result of difficult decisions made by earlier Congresses. These decisions, taken at different points and maintained over time, ultimately helped us to slay the deficit dragon. They included a budget control regimen that imposed caps on discretionary spending and a pay-as-you-go process on budget decisions. The difficult spending and tax decisions that began this process combined to reinforce this fiscal discipline.

As these processes and measures took hold, little by little, deficits receded. As the unified budget went into surplus, a bipartisan consensus emerged on saving the Social Security surpluses. This consensus has also played an important role in today's favorable fiscal outlook and reduced levels of debt held by the public.

Both the Office of Management and Budget (OMB) and CBO project not only Social Security surpluses but also rising levels of non-Social Security, or on-budget, surpluses during the next 10 years. It is these projected surpluses that have changed the budget landscape dramatically since even a year ago.

The surpluses offer a welcome opportunity to address the legitimate, pent-up demands held in abeyance during the era of deficits. At the same time, the surplus estimates imply that, absent policy or economic change, debt held by the public could be virtually eliminated by the end of this decade. As Chairman Greenspan recently emphasized in testimony before this Committee, the possible elimination of publicly held debt is an unexpected aspect of the new budgetary environment. In modern times, it is unprecedented.

The question before this Congress is how to balance today's wants and needs against our long-term challenges. The advent of actual and projected surpluses provides a window to respond to a wide range of demands that were deferred during years of restraint. The surplus does not, however, end our obligation to be prudent in dealing with the taxpayers' dollars. As GAO noted in its January 2001 Performance and

Accountability Series, the newfound budget surpluses provide an opportunity—to move from a focus on annual budget deficits to a reexamination of what government does and how government does business.

Although we can rejoice at the prospect of burgeoning surpluses, we also need to proceed with a measure of caution. It is important to remember that it wasn't that long ago that OMB and CBO projected deficits as far as the eye could see. I do not say this to question the new projections but simply to remind us of their limitations and how they are meant to be used.

In my view, these surpluses also present us with both an opportunity and an obligation. Much of the discussion will properly concern the opportunities that the surpluses afford, but it is important to remember that they bring with them a stewardship obligation. By stewardship obligation, I mean that today's budget decisions need to be made with the future in mind. We must not only respond to the legitimate needs of today but also take into account the longer-term fiscal pressures that will loom ever larger in coming decades as the nation ages and the baby boomers retire.

The message from our long-term budget simulations, which incorporate CBO's 10-year estimates, remains the same as it was even a year ago: even if all the projected, unified surpluses are saved and used for debt reduction, deficits reappear by about 2040. If only the Social Security surpluses are saved, unified deficits emerge by 2020. In both scenarios, deficits would grow to unsustainable levels absent significant policy changes.

To move into the future with no changes in federal health and retirement programs is to envision a very different role for the federal government. Assuming, for example, that Congress and the President adhere to the oft-stated goal of saving the Social Security surpluses but use the on-budget surplus for tax cuts and spending increases, our long-term model shows a world by 2030 in which Social Security, Medicare, and Medicaid increasingly absorb most available revenues within the federal budget. Under this scenario, these programs alone would require more than threequarters of total federal revenue, thereby creating significant pressure to dramatically cut discretionary spending or raise taxes.

Clearly, substantive reform of Social Security and health programs remains critical to recapturing our future fiscal flexibility. Otherwise, little room will be left for other federal spending priorities, such as national defense, education, and law enforcement. Without changes to the structure of Social Security and Medicare, some time during the 2040s government would do nothing but mail checks to the elderly and their health care providers.

These long-term pressures, which cast a shadow on today's budgetary deliberations, pose a new kind of fiscal risk. Budget policy actions must be considered in terms of both their short-term impact and their long-term implications. GAO's work on budget choices in states and in other nations suggests an array of fiscal actions that may serve as a framework for thinking about budget choices in a time of surplus.

The allocation of these surpluses among debt reduction, new or increased spending, and tax cuts is inherently a matter for political choice. However, these choices can be made in the context not only of today's needs but also of future realities. Policymakers should consider a portfolio of actions in which a balanced approach may spread and moderate any related fiscal risk.

America's unprecedented prosperity has put us in a unique position—one with obvious benefits but also very real challenges, especially when it comes to long-term fiscal risk. The surpluses offer policymakers an opportunity to strike a balance between meeting today's needs and meeting the obligation to hand a strong economy and sustainable fiscal policies on to our children, our grandchildren, and generations yet to come.

BIOGRAPHY OF DAVID M. WALKER

David M. Walker became the seventh Comptroller General of the United States and began his 15-year term when he took his oath of office on November 9, 1998. As Comptroller General, Mr. Walker is the nation's chief accountability officer and the head of the General Accounting Office (GAO), a legislative branch agency founded in 1921. GAO helps Congress maximize the performance and ensure the accountability of the federal government for the benefit of the American people. Immediately prior to his appointment as Comptroller General, Mr. Walker was a partner and global managing director of Arthur Andersen LLP's human capital services practice and a member of the board of Arthur Andersen Financial Advisors, a registered investment advisor. He also served as a Public Trustee for Social Security and Medicare from 1990 to 1995, while he was a partner with Arthur Andersen. Before joining Arthur Andersen, Mr. Walker was Assistant Secretary of Labor for Pension and Welfare Benefit Programs and Acting Executive Director for the Pension Benefit Guaranty Corporation. His earlier technical, professional, and business experience was gained with Price Waterhouse, Coopers & Lybrand, and with Source Services Corporation. Mr. Walker is a certified public accountant. He has a B.S. degree in accounting from Jacksonville University and a Senior Management in Government Certificate in Public Policy from the John F. Kennedy School of Government at Harvard University. He is married to the former Mary Etheredge, and they have two adult children—a daughter, Carol, and a son, Andy.

For more information about GAO,
visit our website at

WWW.GAO.GOV

441 G Street, NW
Washington, D.C. 20548